

DEPARTMENT OF THE TREASURY

31 CFR Part 103

RIN: 1506-AB02

Financial Crimes Enforcement Network: Anti-Money Laundering Program and Suspicious Activity Report Filing Requirements for Residential Mortgage Lenders and Originators

AGENCY: Financial Crimes Enforcement Network (“FinCEN”), Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: FinCEN, a bureau of the Department of the Treasury (“Treasury”), is issuing proposed rules defining non-bank residential mortgage lenders and originators as loan or finance companies for the purpose of requiring them to establish anti-money laundering programs and report suspicious activities under the Bank Secrecy Act.

DATES: Written comments on this notice of proposed rulemaking (“NPRM”) must be submitted on or before [INSERT DATE 60 DAYS AFTER PUBLICATION IN THE FEDERAL REGISTER].

ADDRESSES:

FinCEN: You may submit comments, identified by Regulatory Identification Number (RIN) 1506-AB02, by any of the following methods:

- Federal E-rulemaking Portal: <http://www.regulations.gov>. Follow the instructions for submitting comments. Include 1506-AB02 in the submission. Refer to Docket Number FINCEN-2010-0001.
- Mail: FinCEN, P.O. Box 39, Vienna, VA 22183. Include 1506-AB02 in the body of the text. Please submit comments by one method only. Comments submitted

in response to this NPRM will become a matter of public record. Therefore, you should submit only information that you wish to make publicly available.

Inspection of comments: Public comments received electronically or through the U.S. Postal Service sent in response to a notice and request for comment will be made available for public review as soon as possible on www.regulations.gov. Comments received may be physically inspected in the FinCEN reading room located in Vienna, Virginia. Reading room appointments are available weekdays (excluding holidays) between 10 a.m. and 3 p.m., by calling the Disclosure Officer at (703) 905-5034 (not a toll-free call).

FOR FURTHER INFORMATION CONTACT: The FinCEN regulatory helpline at (800) 949-2732 and select Option 6.

SUPPLEMENTARY INFORMATION:

I. Background

The Bank Secrecy Act (“BSA”)¹ authorizes the Secretary of the Treasury (the “Secretary”) to issue regulations requiring financial institutions to keep records and file reports that the Secretary determines “have a high degree of usefulness in criminal, tax, or regulatory investigations or proceedings, or in the conduct of intelligence or counterintelligence activities, including analysis, to protect against international terrorism.”² In addition, the Secretary is authorized to impose anti-money laundering

¹ “Bank Secrecy Act” is the name that has come to be applied to the Currency and Foreign Transactions Reporting Act (Titles I and II of Pub. L. 91-508), its amendments, and the other statutes referring to the subject matter of that Act. These statutes are codified at 12 U.S.C. § 1829b, 12 U.S.C. §§ 1951-1959, and 31 U.S.C. §§ 5311-5314 and 5316-5332, and notes thereto.

² 31 U.S.C. § 5311.

program requirements on financial institutions.³ The authority of the Secretary to administer the BSA has been delegated to the Director of FinCEN.⁴

A. Anti-Money Laundering Programs

Financial institutions are required to establish anti-money laundering (“AML”) programs that include, at a minimum: (1) the development of internal policies, procedures, and controls; (2) the designation of a compliance officer; (3) an ongoing employee training program; and (4) an independent audit function to test programs.⁵ When prescribing minimum standards for AML programs, FinCEN must “consider the extent to which the requirements imposed under [the AML program requirement] are commensurate with the size, location, and activities of the financial institutions to which such regulations apply.”⁶

The BSA defines the term “financial institution” to include, in part, “a loan or finance company.”⁷ On April 29, 2002, and again on November 6, 2002, FinCEN temporarily exempted this category of financial institution, among others, from the requirement to establish an AML program.⁸ The purpose of the temporary exemption was to enable Treasury and FinCEN to study the exempted categories of institutions and to consider the extent to which AML requirements should be applied to them, taking into account their specific characteristics and money laundering vulnerabilities.

³ 31 U.S.C. § 5318(h).

⁴ See Treasury Order 180-01 (Sept. 26, 2002).

⁵ 31 U.S.C. § 5318(h).

⁶ Pub. L. 107-56 § 352(c), 115 Stat. § 322, codified at 31 U.S.C. § 5318 note. Pub. L. 107-56 is the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (“USA PATRIOT Act”).

⁷ 31 U.S.C. § 5312(a)(2)(P).

⁸ See 31 CFR 103.170; 67 FR 21113 (Apr. 29, 2002), as amended at 67 FR 67549 (Nov. 6, 2002) and corrected at 67 FR 68935 (Nov. 14, 2002).

The statutory mandate that all financial institutions establish an anti-money laundering program is a key element in the national effort to prevent and detect money laundering and the financing of terrorism. This NPRM proposes to apply the AML program requirement to companies performing specified services in connection with residential mortgages. This would put these institutions on par with depository institutions performing such services in this respect.⁹

B. Suspicious Activity Reporting Programs

With the enactment of 31 U.S.C. 5318(g) in 1992,¹⁰ Congress authorized the Secretary to require financial institutions to report suspicious transactions. As amended by the USA PATRIOT Act, subsection (g)(1) states:

The Secretary may require any financial institution, and any director, officer, employee, or agent of any financial institution, to report any suspicious transaction relevant to a possible violation of law or regulation.

There has been a regulatory gap between the BSA's coverage of depository institutions and residential mortgage lenders and originators in that the latter are currently not subject to BSA requirements, the Suspicious Activity Report ("SAR") foremost among them. Imposing a SAR requirement would address this regulatory gap. Moreover, a SAR requirement would potentially expand the kinds of activities being reported to FinCEN's BSA database, thereby giving our regulatory and law enforcement partners a more complete picture, both on a systemic and case-specific level, of mortgage-related financial crimes. In these and other respects, residential mortgage lenders and originators

⁹ See 31 CFR 103.120.

¹⁰ 31 U.S.C. 5318(g) was added to the BSA by section 1517 of the Annunzio-Wylie Anti-Money Laundering Act, Title XV of the Housing and Community Development Act of 1992, Pub. L. 102-550; it was expanded by section 403 of the Money Laundering Suppression Act of 1994 (the Money Laundering Suppression Act), Title IV of the Riegle Community Development and Regulatory Improvement Act of 1994, Pub. L. 103-325, to require designation of a single government recipient for reports of suspicious transactions.

may assume an increasingly crucial role in government and industry efforts to protect consumers, mortgage finance businesses, and the U.S. financial system from money laundering and other financial crimes.

C. Regulatory Background

On April 10, 2003, FinCEN issued an advance notice of proposed rulemaking (“ANPRM”) regarding AML requirements for “persons involved in real estate closings and settlements” (“2003 ANPRM”).¹¹ The 2003 ANPRM noted that the BSA had no definition of the term “persons involved in real estate closings and settlements;” that FinCEN had not had occasion to define the term in a regulation; and that the legislative history of the term provided no insight into how Congress intended the term to be defined.

The 2003 ANPRM noted that real estate transactions could involve multiple “persons” (*i.e.*, individuals and business entities), including: real estate agents, banks, mortgage banks, mortgage brokers, title insurance companies, appraisers, escrow agents, settlement attorneys or agents, property inspectors, and other persons directly and tangentially involved in property financing, acquisition, settlement, and occupation. The 2003 ANPRM further noted that persons involved in real estate transactions, and the nature of their involvement, could vary with the contemplated use of the real estate, the nature of the rights to be acquired, or how these rights were to be held, *e.g.*, for residential, commercial, portfolio investment, or development purposes.

The 2003 ANPRM also expressed FinCEN’s views as to guiding principles that should be considered in defining persons involved in real estate closings and settlements.

¹¹ See 68 FR 17569 (Apr. 10, 2003). This category of financial institution is listed at 31 U.S.C. § 5312(a)(2)(U).

Any definitions or terms that define the scope of the rule should consider: (1) those persons whose services rendered or products offered in connection with a real estate closing or settlement can be abused by money launderers; (2) those persons who are positioned to identify the purpose and nature of the transaction; (3) the importance of various participants to successful completion of the transaction, which may suggest that they are well positioned to identify suspicious conduct; (4) the degree to which professionals may have very different roles, in different transactions, which may result in greater exposure to money laundering; and (5) involvement with the actual flow of funds used in the transaction.¹² FinCEN has not issued any additional notices regarding persons involved in real estate closings and settlements since the 2003 ANPRM. FinCEN has, in the interim, continued its research and analysis related to the various categories of financial institutions exempted in 2002.

In view of increasing concern among regulators, law enforcement, and Congress over abusive and fraudulent sales and financing practices in residential mortgage markets, FinCEN has undertaken a number of strategic, outreach, and law enforcement support initiatives and analytical reports related to mortgage fraud.¹³

On July 21, 2009, FinCEN issued an ANPRM entitled “Anti-Money Laundering Program and Suspicious Activity Report Requirements for Non-Bank Residential Mortgage Lenders and Originators.”¹⁴ The 2009 ANPRM expressed FinCEN’s inclination to develop AML and SAR program regulations for a specific subset of loan

¹² See 68 FR 17569, 17570 (Apr. 10, 2003).

¹³ See Mortgage Fraud (a listing of FinCEN’s mortgage fraud related initiatives) www.fincen.gov/mortgagefraud. See also, remarks of James H. Freis, Jr., Director, FinCEN, delivered at the ABA/ABA Money Laundering Enforcement Conference, Oct. 13, 2009 (the “Initiatives Speech”), www.fincen.gov/news_room/speech/html/20071022. See also, remarks of Timothy Geithner, Secretary, U. S. Department of the Treasury, on “The Financial Fraud Enforcement Task Force”, Nov. 17, 2009, www.fincen.gov/whatsnew/html/20091117.

¹⁴ 74 FR 35830 (July 21, 2009) (“2009 ANPRM”).

and finance companies: non-bank residential mortgage lenders and originators.¹⁵ The 2009 ANPRM suggested that any new rules likely would contain standards and requirements analogous to those currently applicable to federally regulated depository institutions.¹⁶

D. Key Issues Related to Proposed AML and SAR Regulations for Residential Mortgage Lenders and Originators

With this NPRM, FinCEN is proposing an incremental approach to implementation of AML and SAR regulations for loan and finance companies that would focus first on those business entities that are engaged in residential mortgage lending or origination and are not currently subject to any AML or SAR program requirement under the BSA. Residential mortgage lenders and originators (*e.g.*, independent mortgage loan companies and mortgage brokers) are primary providers of mortgage finance – in most cases dealing directly with the consumer – and are in a unique position to assess and identify money laundering risks and fraud while directly assisting consumers with their financial needs and protecting them from the abuses of financial crime. FinCEN believes that new regulations requiring residential mortgage lenders and originators to adopt AML programs and report suspicious transactions would augment FinCEN’s initiatives in this area. Among other benefits, such regulations would complement efforts underway by these companies to comply with the nationwide licensing system and registry under development since the passage of the Secure and Fair Enforcement for Mortgage

¹⁵ Id. See also note 7, *supra*. In this case, and throughout this NPRM, the term “residential mortgage originator” is defined to include, among other persons, entities commonly referred to as brokers in the residential mortgage sector.

¹⁶ See 74 FR at 35831.

Licensing Act of 2008 (“SAFE Act”).¹⁷ As mortgage companies and brokers implement systems and procedures to comply with the SAFE Act, there will be opportunities for them to review and enhance their educational and training programs to ensure that employees are able to identify and deal with fraud, money laundering, and other financial crimes appropriately.

In the 2009 ANPRM, FinCEN sought public comment on a wide range of issues, including: (1) the incremental approach to the issuance of regulations for loan and finance companies that would initially affect only those businesses engaged in residential mortgage lending or origination; (2) how any such regulations should define businesses engaged in residential mortgage lending or origination; (3) the financial crime and money laundering risks posed by such businesses; (4) how AML programs for such businesses should be structured; (5) whether such businesses should be covered by BSA requirements other than the AML program requirement and the SAR reporting requirement; and (6) whether certain businesses or transactions should be exempted from AML program or SAR reporting requirements. By issuing this NPRM, FinCEN again requests comments on these issues, this time in the context of a specific proposed regulation, as well as on the matters addressed below.

FinCEN received twelve comments on the 2009 ANPRM: one from the U. S. Department of Justice; five from trade associations; one from a Federal credit union; one from a mortgage company; one from a U.S. Senator; and three from individuals writing on their own behalf.¹⁸ The 2009 ANPRM sought information on a number of key issues

¹⁷ See Title V of Division A of the Housing and Economic Recovery Act of 2008, Pub. L. No. 110-289, 122 Stat. 2810 (2008), codified at 12 U.S.C. §§ 5101, et. seq.

¹⁸ Comments to the 2009 ANPRM are available for public viewing at www.regulations.gov.

related to the possible implementation of AML and SAR program regulations for the sector.

1. Risks of Mortgage Fraud and Money Laundering

As noted in the 2009 ANPRM and the 2003 ANPRM, the residential real estate sector may be vulnerable at all stages of the money laundering process. Money laundering is a process by which the illicit origin of funds is obscured, and a plausible legitimate origin often substituted.¹⁹ The crime of money laundering is defined, in part, with respect to the proceeds of specific unlawful “predicate” activities. Both mortgage fraud and the act of laundering mortgage fraud proceeds are crimes, and both are destructive to consumers, individual businesses and the financial system as a whole. Despite the relative illiquidity of most real estate assets, money launderers have used residential mortgage transactions – fraudulently and legitimately structured – to disguise the proceeds of crime.

In recent years, a significant percentage of SARs filed with FinCEN have reported suspected fraud schemes involving real estate lenders, brokers, agents, appraisers, and other businesses associated with real estate finance and settlements.²⁰ FinCEN studies

¹⁹ There are three general stages of money laundering: placement, layering, and integration. The “placement” stage is the stage at which funds from illegal activity or funds intended to support illegal activity are first introduced into the financial system. Money laundering “layering” involves the distancing of illegal funds from their criminal source through the creation of complex layers of financial transactions. “Integration” occurs when illegal funds are made to appear to have been derived from a legitimate source.

²⁰ See Advisory to Financial Institutions on Filing Suspicious Activity Reports Regarding Home Equity Conversion Mortgage Fraud Schemes, Apr. 2010, www.fincen.gov/statutes_regs/guidance/htm/fin-2010-a005.html; Mortgage Loan Fraud Update, Feb. 2010, www.fincen.gov/news_room/nr/pdf/20100218.pdf; Filing Trends in Mortgage Loan Fraud, Feb. 2009, http://www.fincen.gov/news_room/nr/pdf/20090225a.pdf; Mortgage Loan Fraud: an Update of Trends Based upon Analysis of Suspicious Activity Reports, Apr. 2008, http://www.fincen.gov/news_room/rp/files/MortgageLoanFraudSARAssessment.pdf; Suspected Money Laundering in the Residential Real Estate Industry, Apr. 2008, http://www.fincen.gov/news_room/rp/files/MLR_Real_Estate_Industry_SAR_web.pdf; Money Laundering in the Commercial Real Estate Industry; Dec. 2006,

also have shown the connection between businesses involved in mortgage fraud and other suspected financial crimes.²¹

There was broad agreement among the comments submitted on the 2009 ANPRM that the risks of fraud and other financial crimes, including money laundering, are substantial in the non-bank mortgage finance sector and growing. Some comments stated that the financial crime risks in the sector are “no less significant” than those faced by banks providing mortgage loan services. A few comments stated that the primary risk in the sector is mortgage fraud, and that the risk of money laundering, specifically, is lower than for fraud. Such comments notwithstanding, the proceeds of any mortgage fraud have a high likelihood of being laundered through other financial institutions subject to the BSA, either directly in conjunction with the granting of the mortgage loan and related settlement transactions or at a later stage in conjunction with the placement, layering or integration of proceeds connected with the mortgage fraud.²² FinCEN requests comments that address the experience of the residential mortgage lending sector with money laundering and fraud schemes generally. FinCEN specifically requests information regarding the existence of any safeguards in the sector to guard against fraud, money laundering, and other financial crime, and the applicability of such safeguards to the development of AML and SAR reporting programs.

http://www.fincen.gov/news_room/rp/reports/pdf/CREassessment.pdf; Mortgage Loan Fraud: An Industry Assessment Based Upon Suspicious Activity Report Analysis, Nov. 2006, http://www.fincen.gov/news_room/rp/reports/pdf/mortgage_fraud112006.pdf.

²¹ See Mortgage Loan Fraud Connections with Other Financial Crime: An Evaluation of Suspicious Activity Reports Filed by Money Services Businesses, Securities and Futures Firms, Insurance Companies and Casinos, Mar. 2009, http://www.fincen.gov/news_room/rp/files/mortgage_fraud.pdf.

²² Id.

2. An Incremental Approach to the Sector: Starting With Residential Mortgage Lenders and Originators

As is the case with the term “persons involved in real estate closings and settlements,” the term “loan or finance company” is not defined or discussed in any FinCEN regulation, and there is no legislative history on the term. The term, however, could conceivably extend to any business entity that makes loans to or finances purchases on behalf of consumers and businesses. Loan and finance companies originate loans and leases to finance the purchase of consumer goods such as automobiles, furniture, and household appliances. They also extend personal loans and loans secured by real estate mortgages and deeds of trust, including home equity loans. They supply short- and intermediate-term credit for such purposes as the purchase of equipment and motor vehicles and the financing of inventories. In addition, specialized wholesale loan and finance companies provide liquidity that allows retail loan and finance companies, as well as banks and others, to service end users.²³

Comments submitted on the 2009 ANPRM expressed general support for an incremental approach. One commenter emphasized that the sector has been the primary focus of recent government-wide law enforcement anti-fraud programs. Another commenter expressed the view that most if not all state regulators of mortgage companies likely would support FinCEN’s proposal. While the comments expressed general support for an incremental approach, there also was some concern voiced about limiting the scope

²³ The North American Industry Classification System (“NAICS”) classifies approximately 10 types of mortgage finance related businesses and professions and over 60 other businesses, professions and institutions (*e.g.*, consumer and commercial finance companies, pawnshops, auto finance, equipment leasing, personal credit companies, industrial loan companies and government sponsored enterprises) as primarily engaged in consumer and commercial lending and finance. NAICS was developed as the standard for use by federal statistical agencies in classifying business establishments for the collection, analysis, and publication of statistical data related to the business economy of the U.S. NAICS was developed under the auspices of the Office of Management and Budget (“OMB”), and adopted in 1997.

of the rules to residential mortgage lenders and originators at this time. A few commenters cautioned that FinCEN should not delay implementation of rules for other consumer and commercial finance companies and one commenter urged FinCEN to implement such requirements for persons involved in real estate closings and settlements.

Arguably, the absence of rules for these other types of loan or finance companies might be exploited by criminals insofar as they may shift the focus of their criminal enterprises from residential to other consumer and commercial finance businesses. As noted in the 2009 ANPRM, FinCEN is inclined to defer regulations for commercial real estate finance businesses and other types of consumer and commercial finance businesses until further research and analysis can be conducted to enhance our understanding of the number and kinds of businesses in their sector, their business operations and money laundering vulnerabilities. For the same reasons, FinCEN is not inclined at this time to propose rules for real estate agents and other persons involved in real estate closings and settlements.

FinCEN will continue to study a range of consumer and commercial finance companies with a view toward determining the extent to which it is appropriate to expand the scope of the definition of loan or finance company proposed in this NPRM in a future rulemaking. FinCEN seeks general comment on the application of AML program and SAR regulations to other loan and finance companies. FinCEN requests comment on how new AML and SAR program requirements could be integrated into existing compliance and anti-fraud programs of such companies.

3. Scope of the Rules; Loan or Finance Company

As noted above, “Loan or Finance Company” is a term that could encompass many categories of entities. At this time, FinCEN is only addressing residential mortgage lenders and originators, but future rulemakings may include other types of loan or finance companies. A loan or finance company does not include banks or persons registered with and functionally regulated or examined by the Securities and Exchange Commission or the Commodity Futures Trading Commission, all of which are already subject to AML program and SAR reporting requirements. Additionally, a loan or finance company does not include an individual employed by a loan or finance company or other financial institution. FinCEN does not seek to obligate individuals, but rather businesses, including sole proprietorships, because enterprise wide anti-money laundering programs are more effective and reduce duplicative efforts.

4. Scope of the Rules; Residential Mortgage Lender or Originator

The challenge for FinCEN in drafting rules is that most real estate finance – both residential and commercial – involves complex transactions and multiple parties whose roles are not always readily discernable by the titles and terms used to describe them in generally accepted business practices or under applicable licensing and registration regimes. The primary mortgage market in the United States is fragmented, and even simple real estate finance transactions may involve one or more parties that may originate, fund, broker, purchase, transfer, service, securitize, or insure the mortgage loan. Additionally, the market is fragmented between different types of entities, some of which are already regulated financial institutions, such as banks, and some of which are small independent entities, such as many mortgage brokers.

FinCEN believes that the views, assumptions and guiding principles noted in the 2003 ANPRM are equally relevant to the development of AML program and SAR reporting regulations for residential mortgage lenders and originators. In the 2009 ANPRM and the 2003 ANPRM, FinCEN stated that AML obligations should be applicable to those persons that “conduct the activities that place them in the best position to identify the nature of the transaction, recognize suspicious activity, and prevent misuse of their services for money laundering and other financial crimes.”²⁴ This activity-based approach focuses on the nature of the activity conducted and its primary function in a particular residential mortgage transaction, rather than on the name or title ascribed to the person facilitating the transaction.

Comments on the 2009 ANPRM reflected broad agreement that the definitions should be crafted so that the rules encompass an appropriate range of key non-bank residential mortgage lenders and originators. FinCEN seeks comment on which participants involved in non-bank residential mortgage finance are in a position where they can effectively identify and guard against fraud, money laundering, and other financial crimes. Commenters may, among other things, address both the extent to which various participants have access to information regarding the nature and purpose of the transactions at issue and the importance of the participants’ involvement to successful completion of the transactions. Comments are welcome from those involved centrally in the residential mortgage finance process (*i.e.*, those who may act as an agent for some or all of the parties and are responsible for reviewing the form and type of payment, as well as being aware of the parties to the mortgage transaction), and those who view their involvement as more peripheral. FinCEN seeks comment specifically on whether

²⁴ 2009 ANPRM, 74 FR at 35833.

FinCEN should adopt the definitions of “residential mortgage lender,” “residential mortgage originator,” and “residential mortgage loan” set forth in the proposed regulation at 103.11(ddd).²⁵

5. Scope of the Rules; Entities not Covered by the Definitions

The proposed definitions do not include natural persons and certain businesses and transactions, described below.²⁶ FinCEN therefore requests comment on whether the definitions used should be wider or narrower in scope to include or exclude any specific types of residential mortgage lenders or originators or any specific category of mortgage finance customer or transaction. Two commenters on the 2009 ANPRM expressed the view that any new rules should not recognize or permit any exemptions or exceptions. Consistent with FinCEN’s perspective on the issue, several comments submitted on the 2009 ANPRM suggested that any exemptions FinCEN considers should take into account and balance the risks of money laundering against the implementation and compliance costs and obligations likely to be borne by this sector. FinCEN endeavors to balance and take into account the benefits of the regulations (including the prevention and detection of money laundering and other financial crimes, as well as the value to law enforcement and regulatory agencies of additional data on suspected financial crimes) against the implementation and compliance costs and obligations likely to be borne by the industry.

One comment submitted on the 2009 ANPRM stated that individuals in seller-financed transactions should be excluded from the scope definitions, or exempt from the

²⁵ As noted in the 2009 ANPRM, several definitions in current federal law (*e.g.*, definitions of “mortgage lending business” and “loan originator”) may be useful references for comments on the scope of the proposed regulations. See 74 FR at 35833.

²⁶ The proposed regulations apply to businesses, including sole proprietorships, not individuals. Thus, for example, individuals covered by the SAFE Act definition of “loan originator,” 12 U.S.C. § 5102(3)(A)(ii), would not be covered by the proposed regulations.

rules. FinCEN agrees, and this NPRM proposes exemptions for individuals financing the sale of their own real estate. Two comments on the 2009 ANPRM suggested that persons conducting a *de minimis* number of transactions – as few as one and as many as five were suggested – should be carved out of the scope definitions or exempt. At this time, FinCEN does not intend to propose an exemption for a person that conducts or facilitates a relatively low volume of mortgage finance transactions if the person nonetheless falls within the definition of residential mortgage lender or originator. FinCEN intends the proposed regulations to reflect the distinction between a seller-financed transaction (which typically involves family members or friends in a one-time transaction) and a person that is primarily engaged in the mortgage finance business but for business reasons or changes in markets, competition or other factors, conducts relatively few transactions within a given period.

The proposed definitions also do not include those persons that are solely responsible for administrative functions that support or facilitate residential mortgage finance transactions. FinCEN requests comment on whether it is necessary for FinCEN to provide a specific exemption for persons performing administrative support functions. Such an exemption would be consistent with the SAFE Act, which recognizes an administrative support exemption or carve-out from the definition of “loan originator.”²⁷ FinCEN seeks comment on whether other specific businesses or transactions should be excluded from the definition of loan or finance company.

Comments regarding the scope of the definitions should be designed to enable FinCEN to evaluate the risks of money laundering, the potential value to law enforcement, and other relevant factors. FinCEN also seeks suggestions on how FinCEN

²⁷ See 12 U.S.C. § 5102(3)(A)(ii).

may craft clearly delineated categories of included and excluded businesses or transactions.

6. Structure and Elements of AML and SAR Regulations

The 2009 ANPRM stated FinCEN's inclination to propose AML and SAR rules that have similar reporting standards, thresholds, and procedures to those set forth in AML and SAR regulations for other industries. The proposed AML and SAR rules contain essentially the same standards and requirements as the existing BSA rules for other financial institutions.

FinCEN has promulgated SAR reporting regulations for a number of financial institutions that have AML program requirements, including: mutual funds, insurance companies, futures commission merchants and introducing brokers in commodities, banks, brokers or dealers in securities, money services businesses, and casinos.²⁸

In applying the AML program requirements to residential mortgage lenders and originators, FinCEN must consider the extent to which the standards for AML programs are commensurate with the size, location, and activities of such persons.²⁹ FinCEN recognizes that while large businesses are engaged in mortgage finance, businesses in this industry may also include smaller companies or sole proprietors. FinCEN thus seeks comment on any particular concerns smaller businesses may have regarding the implementation of AML and SAR reporting programs.

FinCEN believes that AML programs will complement the anti-fraud and general compliance programs that residential mortgage lenders and originators have established to comply with the SAFE Act and other federal and state laws and protect their own

²⁸ See 31 CFR 103.15 – 103.21.

²⁹ See note 6, *supra*.

business operations. Many residential mortgage lenders and originators may be able to integrate risk-based AML reporting programs into existing enterprise-wide, anti-fraud, and compliance programs in a complementary manner that utilizes efficiencies and commonalities and enhances the effectiveness of a business's compliance measures. As noted, these businesses also may have procedures in place to prevent fraud, which they may be able to integrate into their AML programs.³⁰ FinCEN seeks comment on how the programs and practices that residential mortgage lenders and originators have in place to prevent mortgage fraud and other illegal activities may be applicable to the development of AML and SAR programs.

Accordingly, in this NPRM, FinCEN proposes AML and SAR regulations applicable to residential mortgage lenders and originators that contain similar reporting standards, thresholds, and procedures to those set forth in AML and SAR regulations for other industries. As FinCEN has emphasized in its recent reports on mortgage loan fraud trends, SARs provide a valuable tool for regulatory and law enforcement agencies seeking to isolate specific instances of potential criminal activity for further investigation, and to identify emerging money laundering and terrorism financing trends.³¹ The due diligence necessary for financial institutions to detect and report known or suspected suspicious activity greatly reduces vulnerability to the abuses of money laundering and terrorist financing.

In response to the 2009 ANPRM, one law enforcement agency stated that the absence of SAR data from the sector has impeded law enforcement analysis of mortgage fraud and related crimes. Several comments agreed that SARs provide important, timely

³⁰ See Initiatives Speech, page 4.

³¹ See Filing Trends in Mortgage Loan Fraud, Feb. 2009, page 1, http://www.fincen.gov/news_room/nr/pdf/20090225a.pdf.

information to help investigate and prosecute financial crimes and that mortgage lenders should be required to file SARs. Three major trade associations stated that mortgage lenders and originators are in a unique position to identify and report mortgage-related money laundering and fraud.

Several commenters urged FinCEN to propose only AML and SAR program requirements for the sector at this time. Because FinCEN believes an incremental approach is appropriate, FinCEN defers proposing additional BSA regulations for the sector at this time, including Currency Transaction Report (CTR) requirements. Entities subject to this regulation would still have to file Form 8300 for transactions involving the receipt of more than \$10,000 in currency. However, FinCEN may determine, after further research, that additional BSA regulations may be appropriate for this sector. FinCEN seeks comment on whether it should consider other BSA regulations in addition to AML program and SAR requirements.

FinCEN seeks general comment regarding the impact of the proposed new rules, specifically: (1) the impact of AML or SAR regulations on business operations, profitability, growth and practices; (2) the impact of AML or SAR regulations or other BSA regulations on consumers seeking to obtain residential mortgages; (3) the effectiveness of examining for and enforcing compliance with any such regulatory requirements; and (4) the advisability of establishing some minimum transaction threshold value or annual volume threshold below which some or all regulatory requirements would not apply. We also solicit comment on the value to law enforcement and regulatory agencies of the proposed regulations. Comments on all aspects of the NPRM are welcome, and we encourage all interested parties to provide their views.

7. Consideration of Examination Authority

Generally, the Internal Revenue Service has been delegated the authority to examine for BSA compliance purposes those regulated entities without a federal functional regulator with broad supervisory authority.³² FinCEN seeks comment on any particular aspects of the loan or finance company sector that should be considered when making a decision about whether, to whom, and how to delegate examination authority. FinCEN also seeks comment on how frequently, to what extent, and for compliance with what laws and regulations loan or finance companies are examined by various state or other regulators and whether such examination processes may be relied on or otherwise used to help in examination for compliance with the BSA.

II. Section-by-Section Analysis

A. Definition of Loan or Finance Company

Section 103.11(ddd) defines the key terms used in the proposed rules. The definitions reflect FinCEN's determination that the term "loan or finance company" should be limited, at this time, to residential mortgage lenders and originators, and that AML program and SAR requirements should be applied first to these businesses, and later as part of a phased approach applied to other consumer and commercial loan and finance companies. The definition of a loan or finance company includes entities that engage in activities within the United States, whether or not through an agent, agency, branch or office, and does not include banks or entities registered with and functionally regulated or examined by the Securities and Exchange Commission or the Commodity Futures Trading Commission. Additionally, a loan or finance company does not include an individual employed by a loan or finance company or other financial institution.

³² See, e.g., 31 CFR 103.56(b)(8).

Residential mortgage lender is defined as “[t]he person to whom the debt arising from a residential mortgage loan is initially payable on the face of the evidence of indebtedness or, if there is no such evidence of indebtedness, by agreement, or to whom the obligation is initially assigned at or immediately after settlement.” The definition specifically excludes an individual who finances the sale of their own dwelling or real property.

Residential mortgage originator is defined as a person who “takes a residential mortgage loan application and offers or negotiates terms of a residential mortgage loan for compensation or gain.”

Residential mortgage loan is defined as any loan “that is secured by a mortgage, deed of trust, or other equivalent consensual security interest” on a 1-to-4 family residential structure or real estate on which a residential structure will be built. This definition is intended to encompass any loan secured by residential real property, regardless of whether the borrower is purchasing the residential real property as a primary residence, vacation home or investment, is refinancing a purchase-money mortgage loan to obtain a more favorable rate and/or terms, or is obtaining a mortgage loan for another purpose, such as debt consolidation or mobilization of home equity. For this definition, residential real property is intended to be a broad category, including condominiums, co-ops, mobile homes intended to be used as dwellings, vacation homes, and time shares.

Comment is specifically invited on whether the above definitions are appropriate in light of money laundering risks in the industry and the strategic and policy goals set forth in this notice and in the 2003 and 2009 ANPRMs. Comment also is specifically

invited on whether the final rule also should require agents and brokers of residential mortgage lenders and originators, or any subsets of agents or brokers, to adopt AML programs and report suspicious transactions. Finally, comment is specifically invited on whether the proposed definition of “residential mortgage loan” manifests with adequate clarity FinCEN’s stated intent for the definition.

B. Reports of Suspicious Transactions

Section 103.14(a) contains the rules setting forth the obligation of loan or finance companies to report suspicious transactions that are conducted or attempted by, at, or through a loan or finance company and involve or aggregate at least \$5,000 in funds or other assets. It is important to recognize that transactions are reportable under this rule and 31 U.S.C. 5318(g) regardless of whether they involve currency. The \$5,000 minimum amount is consistent with existing SAR filing requirements for financial institutions.

Section 103.14(a)(1) contains the general statement of the obligation to file reports of suspicious transactions. The obligation extends to transactions conducted or attempted by, at, or through a loan or finance company. The rule also contains a provision in section 103.14(a)(1) designed to encourage the reporting of transactions that appear relevant to violations of law or regulation, even in cases in which the rule does not explicitly so require, for example in the case of a transaction falling below the \$5,000 threshold in the rule.

Section 103.14(a)(2) specifically describes the four categories of transactions that require reporting. A loan or finance company is required to report a transaction if it knows, suspects, or has reason to suspect that the transaction (or a pattern of transactions

of which the transaction is a part): (i) involves funds derived from illegal activity or is intended or conducted to hide or disguise funds or assets derived from illegal activity; (ii) is designed, whether through structuring or other means, to evade the requirements of the BSA; (iii) has no business or apparent lawful purpose, and the loan or finance company knows of no reasonable explanation for the transaction after examining the available facts; or (iv) involves the use of the loan or finance company to facilitate criminal activity.³³

A determination as to whether a report is required must be based on all the facts and circumstances relating to the transaction and customer of the loan or finance company in question. Different fact patterns will require different judgments. Some examples of red flags associated with existing or potential customers are referenced in previous FinCEN reports on mortgage fraud and money laundering in the residential and commercial real estate sectors.³⁴ However, the means of commerce and the techniques of money laundering are continually evolving, and there is no way to provide an exhaustive list of suspicious transactions. FinCEN will continue to pursue a regulatory approach that involves a combination of guidance, training programs, and government-industry information exchange so that implementation of any new AML program and SAR reporting regulations can be implemented by covered businesses in as flexible and cost efficient way as possible, while protecting the sector and the financial system as a whole from fraud, money laundering and other financial crimes.

³³ The fourth reporting category has been added to the suspicious activity reporting rules promulgated since the passage of the USA PATRIOT Act to make it clear that the requirement to report suspicious activity encompasses the reporting of transactions involving fraud and those in which legally derived funds are used for criminal activity, such as the financing of terrorism.

³⁴ See note 21, *supra*.

Section 103.14(a)(3) provides that the obligation to identify and to report a suspicious transaction rests with the loan or finance company involved in the transaction. However, where more than one loan or finance company, or another financial institution with a separate suspicious activity reporting obligation, is involved in the same transaction, only one report is required to be filed, provided it contains all relevant facts and each institution maintains a copy of the report and any supporting documentation.

The proposed rule is intended to require that a loan or finance company evaluate customer activity and relationships for fraud, money laundering and other financial crime risks, and design a suspicious transaction monitoring program that is appropriate for the particular loan or finance company in light of such risks.

Section 103.14(b) sets forth the filing procedures to be followed by loan or finance companies making reports of suspicious transactions. Within 30 days after a loan or finance company becomes aware of a suspicious transaction, the business must report the transaction by completing a SAR and filing it with FinCEN. Supporting documentation relating to each SAR is to be collected and maintained separately by the loan or finance company and made available to FinCEN or any Federal, state, or local law enforcement agency, or any Federal regulatory authority that examines the loan or finance company for compliance with the BSA, or any state regulatory authority that examines the loan or finance company for compliance with state law requiring compliance with the BSA,³⁵ upon request. Because supporting documentation has been

³⁵ State regulatory authorities are generally authorized by state law to examine for compliance with the BSA in one of two ways: (1) the law authorizes the state authority to examine the institution for compliance with all federal laws and regulations generally or with the BSA explicitly, or (2) the law requires a financial institution to comply with all federal laws and regulations generally or with the BSA explicitly, and authorizes the state authority to examine for compliance with the state law. An institution may provide SAR information to a state regulatory authority meeting either criterion.

deemed to have been filed with the SAR, these parties are consistent with those parties to whom a SAR may be disclosed as discussed in the rules of construction, below. For situations requiring immediate attention, loan or finance companies are to telephone the appropriate law enforcement authority in addition to filing a SAR.

Section 103.14(c) provides that filing loan or finance companies must maintain copies of SARs and the underlying related documentation for a period of five years from the date of filing. As indicated above, supporting documentation is to be made available to FinCEN and the prescribed law enforcement and regulatory authorities, upon request.

Section 103.14(d)(1) reinforces the statutory prohibition against the disclosure by a financial institution of a SAR (regardless of whether the report is required by the proposed rule or is filed voluntarily).³⁶ Thus, the section requires that a SAR and information that would reveal the existence of that SAR (“SAR information”) be kept confidential and not be disclosed except as authorized within the rules of construction. The proposed rule includes rules of construction that identify actions an institution may take that are not precluded by the confidentiality provision. These actions include the disclosure of SAR information to FinCEN, or Federal, state, or local law enforcement agencies, or a Federal regulatory authority that examines the loan or finance company for compliance with the BSA, or a state regulatory authority that examines the loan or finance company for compliance with state law requiring compliance with the BSA.³⁷ This confidentiality provision also does not prohibit the disclosure of the underlying facts, transactions, and documents upon which a SAR is based, or the sharing of SAR information within the loan or finance company’s corporate organizational structure for

³⁶ See 31 U.S.C. 5318(g)(2).

³⁷ See note 38, supra.

purposes consistent with Title II of the BSA as determined by FinCEN in regulation or in guidance.³⁸

Section 103.14(d)(2) incorporates the statutory prohibition against disclosure of SAR information, other than in fulfillment of their official duties consistent with the BSA, by government users of SAR data. The section also clarifies that official duties do not include the disclosure of SAR information in response to a request by a non-governmental entity for non-public information³⁹ or for use in a private legal proceeding, including a request under 31 CFR 1.11.⁴⁰

Section 103.14(e) provides protection from liability for making reports of suspicious transactions, and for failures to disclose the fact of such reporting to the full extent provided by 31 U.S.C. 5318(g)(3).

Section 103.14(f) notes that compliance with the obligation to report suspicious transactions will be examined by FinCEN or its delegates, and provides that failure to comply with the rule may constitute a violation of the BSA and the BSA regulations.

Section 103.14(g) provides that the new SAR requirement applies to transactions occurring after the later of six months from the effective date of a final rule or the establishment of a business entity subject to the rules.

³⁸ On January 20, 2006, FinCEN issued guidance for the banking, securities, and futures industries authorizing the sharing of SAR information with parent companies, head offices, or controlling companies. To date, no such guidance has been issued for the loan or finance industry.

³⁹ For purposes of this rulemaking, “non-public information” refers to information that is exempt from disclosure under the Freedom of Information Act.

⁴⁰ 31 CFR 1.11 is the Department of the Treasury’s information disclosure regulation. Generally, these regulations are known as “Touhy regulations,” after the Supreme Court’s decision in United States ex rel. Touhy v. Ragen, 340 U.S. 462 (1951). In that case, the Supreme Court held that an agency employee could not be held in contempt for refusing to disclose agency records or information when following the instructions of his or her supervisor regarding the disclosure. An agency’s Touhy regulations are the instructions agency employees must follow when those employees receive requests or demands to testify or otherwise disclose agency records or information.

C. Anti-Money Laundering Program

Section 103.142(a) requires that each loan or finance company develop and implement an anti-money laundering program reasonably designed to prevent the loan or finance company from being used to facilitate money laundering or the financing of terrorist activities. The program must be in writing and must be approved by senior management. A loan or finance company's written program also must be made available to FinCEN upon request. The minimum requirements for the AML program are set forth in section 103.142(b). Beyond these minimum requirements, however, the proposed rule is intended to give loan or finance companies the flexibility to design their programs to mitigate their own enterprise-specific risks.

Section 103.142(b) sets forth the minimum requirements of a loan or finance company's AML program. Section 103.142(b)(1) requires the AML program to incorporate policies, procedures, and internal controls based upon the loan or finance company's assessment of the money laundering and terrorist financing risks associated with its products, customers, distribution channels, and geographic locations. As explained above, a loan or finance company's assessment of customer-related information, such as methods of payment, is a key component to an effective AML program. Thus, a loan or finance company's AML program must ensure that the company obtains all the information necessary to make its AML program effective. Such information includes, but is not limited to, relevant customer information collected and maintained by the loan or finance company's agents and brokers. The specific means to obtain such information is left to the discretion of the loan or finance company, although FinCEN anticipates that the loan or finance company may need to amend existing

agreements with its agents and brokers to ensure that the company receives necessary customer information. For purposes of making the required risk assessment, a loan or finance company must consider all relevant information.

Policies, procedures, and internal controls also must be reasonably designed to ensure compliance with BSA requirements. Loan or finance companies may conduct some of their operations through agents and third-party service providers. Some elements of the compliance program may best be performed by personnel of these entities, in which case it is permissible for a loan or finance company to delegate contractually the implementation and operation of those aspects of its AML program to such an entity. Any loan or finance company that delegates responsibility for aspects of its AML program to an agent or a third party, however, remains fully responsible for the effectiveness of the program, as well as ensuring that compliance examiners are able to obtain information and records relating to the AML program.

Section 103.142(b)(2) requires that a loan or finance company designate a compliance officer to be responsible for administering the AML program. A loan or finance company may designate a single person or committee to be responsible for compliance. The person or persons should be competent and knowledgeable regarding BSA requirements and money laundering issues and risks, and should be empowered with full responsibility and authority to develop and enforce appropriate policies and procedures. The role of the compliance officer is to ensure that (1) the program is implemented effectively; (2) the program is updated as necessary; and (3) appropriate persons are trained and educated in accordance with section 103.142(b)(3).

Section 103.142(b)(3) requires that a loan or finance company provide for education and training of appropriate persons. Employee training is an integral part of any AML program. In order to carry out their responsibilities effectively, employees of a loan or finance company (and of any agent or third-party service provider) with responsibility under the program must be trained in the requirements of the rule and money laundering risks generally so that red flags associated with existing or potential customers can be identified. Such training may be conducted by outside or in-house seminars, and may include computer-based training. The nature, scope, and frequency of the education and training program of the loan or finance company will depend upon the employee functions performed. However, those with obligations under the AML program must be sufficiently trained to carry out their responsibilities effectively. Moreover, these employees should receive periodic updates and refreshers regarding the AML program.

Section 103.142(b)(4) requires that a loan or finance company provide for independent testing of the program on a periodic basis to ensure that it complies with the requirements of the rule and that the program functions as designed. An outside consultant or accountant need not perform the test. The review may be conducted by an officer, employee or group of employees, so long as the reviewer is not the designated compliance officer and does not report directly to the compliance officer. The frequency of the independent testing will depend upon the loan or finance company's assessment of the risks posed. Any recommendations resulting from such testing should be implemented promptly or reviewed by senior management.

Section 103.142(c) states that compliance with the AML program requirements will be determined by FinCEN or its delegates, under the terms of the BSA.

III. Proposed Location in Chapter X

As discussed in a previous Federal Register Notice,⁴¹ FinCEN is separately proposing to remove Part 103 of Chapter I of Title 31, Code of Federal Regulations, and add the reorganized contents of Part 103 as new Parts 1000 to 1099 ("Chapter X"). If the notice of proposed rulemaking for Chapter X is finalized, the changes in the present proposed rule would be reorganized according to the proposed Chapter X. The planned reorganization will have no substantive effect on the regulatory changes herein. The regulatory changes of this specific rulemaking would be renumbered according to the proposed Chapter X as follows:

- (a) 103.11 would be moved to 1010.100;
- (b) 103.14 would be moved to 1029.320; and
- (c) 103.142 would be moved to 1029.210.

IV. Regulatory Flexibility Act

When an agency issues a rulemaking proposal, the Regulatory Flexibility Act ("RFA") requires the agency to "prepare and make available for public comment an initial regulatory flexibility analysis," which will "describe the impact of the proposed rule on small entities."⁴² Section 605 of the RFA allows an agency to certify a rule, in lieu of preparing an analysis, if the proposed rulemaking is not expected to have a significant economic impact on a substantial number of small entities.

⁴¹ 73 FR 66414 (Nov. 7, 2008).

⁴² 5 U.S.C. § 603(a).

Estimate of the number of small entities to which the proposed rule will apply:

For the purpose of arriving at an estimated number of residential mortgage lenders and originators, FinCEN is relying on information gathered from various public sources, including major trade associations and associations of government regulators. Estimates based on this data suggest that as of 2010 there are approximately 31,000 qualifying entities in the United States, down from approximately 42,000 in 2009. FinCEN also referred to information gathered from the NAICS codes,⁴³ which lists loan and finance companies as NAICS codes 522292 (Real Estate Credit) and 522310 (Mortgage and Nonmortgage Loan Brokers). The U.S. Census Bureau estimated there were about 36,275 entities in these classifications in 2002. However, these classifications include services that are outside of those provided by loan and finance companies (*i.e.* bank lenders), so the number of loan or finance companies to which this proposed rule is applicable could be significantly less. Within this classification, those entities that have less than 7 million dollars in gross revenue are considered small. FinCEN estimates that 95% of the affected industry is considered a small business, and that the proposed regulation would affect all of them.

Description of the projected reporting and recordkeeping requirements of the proposed rule:

The proposed rule would require loan and finance companies to maintain AML programs and file reports on suspicious transactions. By requiring this, FinCEN is addressing vulnerabilities in the U.S. financial system and is leveling the playing field between bank and non-bank lenders. FinCEN does not foresee a significant impact on the regulated industry from these requirements. Loan or finance companies, as a usual

⁴³ See note 24, *supra*.

and customary part of their business for each transaction, conduct a significant amount of due diligence on both the property securing the loan and the borrower. This process of due diligence involves the types of inquiry and collecting the types of information that would be expected in any program to prevent money laundering and fraud and to detect and report suspicious transactions.⁴⁴

AML Program Requirement in General

The proposed rule would not impose significant burdens on loan and finance companies. These companies may build on their existing risk management procedures and prudential business practices to ensure compliance with this rule. FinCEN and other agencies have issued substantial guidance on the development of AML programs and SAR reporting requirements.⁴⁵ Most loan and finance companies subject to the proposed rule would not need to obtain more sophisticated legal or accounting advice than that already required to run their businesses. Residential mortgage lenders and originators undertake thorough due diligence of borrowers and collateral to assess the credit risk associated with a particular loan. The information gathered by these businesses generally is the same as, or very similar to, the information that would be expected in any programs to prevent money laundering and detect and report suspicious transactions. FinCEN

⁴⁴ See, e.g., Form 1003 Uniform Residential Mortgage Application, available at <https://www.efanniemae.com/sf/formsdocs/forms/pdf/sellingtrans/1003.pdf> or http://www.freddiemac.com/uniform/doc/form_65_urla_7_05.doc.

⁴⁵ See, e.g., Guidance – Preparing a Complete and Sufficient Suspicious Activity Report Narrative (including related PowerPoint Presentation - Keys to Writing a Complete and Sufficient SAR Narrative), Nov. 2003, http://www.fincen.gov/statutes_regs/guidance/html/narrativeguidance_webintro.html ; Guidance – Suggestions for Addressing Common Errors Noted in Suspicious Activity Reporting, Oct. 10, 2007, http://www.fincen.gov/statutes_regs/guidance/html/SAR_Common_Errors_Web_Posting.html ; Guidance – Suspicious Activity Report Supporting Documentation, June 13, 2007 (FIN-2007-G003), http://www.fincen.gov/statutes_regs/guidance/html/Supporting_Documentation_Guidance.html The SAR Activity Review – Trends, Tips and Issues (Issue 16), Oct. 2009, Section 4, *Law Enforcement Suggestions When Preparing Suspicious Activity Reports*, p. 45., http://www.fincen.gov/statutes_regs/guidance/html/narrativeguidance_webintro.html . See also notes 13 and 21, *supra*.

seeks comment on the extent to which AML programs or SAR reporting requirements would require affected businesses to conduct a degree of due diligence, or collect an amount of information, beyond that presently conducted to assess credit worthiness and minimize losses due to fraud.

Finally, FinCEN believes that the flexibility incorporated into the proposed rule would permit each loan or finance company to tailor its AML program to fit its own size and needs. In this regard, FinCEN believes that expenditures associated with establishing and implementing an AML program will be commensurate with the size and risk profile of a loan or finance company. If a loan or finance company is small or does not engage in high risk transactions, therefore, the burden to comply with the proposed rule should be minimal. FinCEN estimates that the impact of this requirement would not be significant.

Suspicious Activity Reporting

The proposed rule would require loan and finance companies to report on transactions of \$5,000 or more which they determine to be suspicious. Loan and finance companies have not been previously required to comply with such a requirement under regulation. However, as noted above, most loan and finance companies, in order to remain viable, have in place policies and procedures to prevent and detect fraud. Such anti-fraud measures should assist loan and finance companies in reporting suspicious transactions. Many loan and finance companies already voluntarily report suspicious transactions and fraud through entities such as the Loan Modification Scam Prevention Network.⁴⁶ Additionally, loan and finance companies, as part of the application process

⁴⁶ The Loan Modification Scam Prevention Network includes Fannie Mae, Freddie Mac, the Lawyers' Committee for Civil Rights Under Law (Lawyers' Committee) and NeighborWorks America, among

for loans, already gather the information necessary to fill out SAR forms as a usual and customary part of their business. It is likely that the software packages most such companies already use will, after this proposed regulation, incorporate the ability to automatically fill out all but the narrative field in a SAR based on information already input for the loan application.⁴⁷ Therefore, FinCEN estimates that the burden of the SAR filing requirements for loan and finance companies would be low.

Certification

The additional burden proposed by the rule would be a requirement to maintain an AML program and a SAR filing requirement. As discussed above, FinCEN estimates that the impact from these requirements would not be significant. Accordingly, FinCEN certifies that the proposed rule would not have a significant impact on a substantial number of small entities.

Questions for Comment:

1. Please provide comment on any or all of the provisions in the proposed rule with regard to (a) the impact of the provision(s) (including any benefits and costs), if any, in carrying out responsibilities under the proposed rule and (b) what less burdensome alternatives if any, FinCEN should consider.

2. Please provide comment regarding whether the AML program and SAR reporting requirements proposed in this rule would require entities to gather any

others, with representatives from key governmental agencies, such as the Federal Trade Commission, the U.S. Department of Housing and Urban Development (HUD), U.S. Department of Justice, the U.S. Treasury Department, the Federal Bureau of Investigation, and state Attorneys General offices, as well as leading non-profit organizations from across the country. See <http://www.preventloanscams.org/>.

⁴⁷ See Form 1003 Uniform Residential Mortgage Application, , available at <https://www.efanniemae.com/sf/formsdocs/forms/pdf/sellingtrans/1003.pdf> or http://www.freddiemac.com/uniform/doc/form_65_urla_7_05.doc.

information not already gathered as part of the due diligence, underwriting, and compliance process and provide specific examples of such information.

V. Paperwork Reduction Act Notices

The collection of information contained in this proposed rule is being submitted to OMB for review in accordance with the Paperwork Reduction Act of 1995 (“PRA”).⁴⁸ Comments on the collection of information should be sent (preferably by fax (202-395-6974)) to Desk Officer for the Department of the Treasury, Office of Information and Regulatory Affairs, Office of Management and Budget, Paperwork Reduction Project (1506), Washington, DC 20503 or by the Internet to OIRA_submission@omb.eop.gov, with a copy to the FinCEN by mail. Comments on the collection of information should be received by [INSERT DATE 60 DAYS FROM DATE OF PUBLICATION IN THE FEDERAL REGISTER]

In accordance with the requirements of the PRA,⁴⁹ and its implementing regulations, 5 CFR 1320, the following information concerning the collection of information is presented to assist those persons wishing to comment on the information collection. The information collections in this proposal are contained in 31 CFR 103.14 and 31 CFR 103.142.

AML program for loan and finance companies.

AML programs for loan and finance companies (31 CFR 103.142). This information would be required to be retained pursuant to 31 U.S.C. 5318(h) and proposed 31 CFR 103.142. The collection of information would be mandatory. The information

⁴⁸ 44 U.S.C. 3507(d).

⁴⁹ See 44 U.S.C. 3506(c)(2)(A).

collected would be pursuant to 103.142 and would be used by examiners to determine whether loan and finance companies comply with the BSA.

Description of Recordkeepers: Loan and finance companies as defined in 31 CFR 103.11(ddd).

Estimated Number of Recordkeepers: 31,000.

Estimated Average Annual Burden Hours per Recordkeeper: The estimated average annual burden associated with the recordkeeping requirement in proposed 31 CFR 103.142 is three hours.

Estimated Total Annual Recordkeeping Burden: FinCEN estimates that the annual recordkeeping burden would be 93,000 hours.

This burden will be included (added to) the existing burden listed under OMB Control Number 1506-0035 currently titled AML Programs for insurance companies. The new title for this control number will become AML Programs for insurance companies and loan and finance companies. The new total burden will 94,200 hours.

SAR filing for loan and finance companies.

SARs for loan and finance companies (proposed 31 CFR 103.14). This information would be required to be provided pursuant to 31 U.S.C. 5318(g) and 31 CFR 103.14. This information would be used by law enforcement agencies in the enforcement of criminal and regulatory laws and to prevent loan and finance companies from engaging in illegal activities. The collection of information is mandatory. The proposal would increase the number of recordkeepers by 31,000.

Description of Recordkeepers: Loan and finance companies as defined in 31 CFR 103.11(ddd).

Estimated Number of Recordkeepers: 31,000.

Estimated Average Annual Burden Hours per Recordkeeper: The estimated average annual burden associated with the recordkeeping requirement in 31 CFR 103.14 is 2 hours per report, and FinCEN estimates that, on average, one report per filer will be filed per year.

Estimated Total Annual Recordkeeping Burden: The proposal would increase the estimated annual burden by 62,000 consisting of one hour for report completion and one hour for required recordkeeping.

This is a new requirement that will require a new OMB Control Number 1506-XXXX.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection of information displays a valid OMB control number. Records required to be retained under the BSA must be retained for five years.

Questions for Comment:

1. We seek comments on FinCEN's three hour recordkeeping estimate for the establishment of AML programs by loan and finance companies; whether this estimate is too low; and, if so, an estimate that better reflects industry practices. We also ask commenters to provide an estimate of costs associated with establishing these AML programs, especially with regards to systems and labor costs.
2. We seek comment on FinCEN's two hour estimate for annual SAR filings by loan and finance companies and whether this estimate is too low. We also ask

commenters to provide an estimate of costs associated with the SAR filing requirement.

VI. Executive Order 12866

It has been determined that this proposed rule is a significant regulatory action for purposes of Executive Order 12866.

VII. Unfunded Mandates Act of 1995 Statement

Section 202 of the Unfunded Mandates Reform Act of 1995 (“Unfunded Mandates Act”), Public Law 104-4 (March 22, 1995), requires that an agency prepare a budgetary impact statement before promulgating a rule that may result in expenditure by the state, local, and tribal governments, in the aggregate, or by the private sector, of \$100 million or more in any one year. If a budgetary impact statement is required, section 202 of the Unfunded Mandates Act also requires an agency to identify and consider a reasonable number of regulatory alternatives before promulgating a rule. Taking into account the factors noted above and using conservative estimates of average labor costs in evaluating the cost of the burden imposed by the proposed regulation, FinCEN has determined that it is not required to prepare a written statement under section 202.

VIII. List of Subjects in 31 CFR Part 103

Administrative practice and procedure, Banks, Banking, Brokers, Currency, Foreign banking, Foreign currencies, Gambling, Investigations, Penalties, Reporting and recordkeeping requirements, Securities, Terrorism.

IX. Authority and Issuance

For the reasons set forth in the preamble, part 103 of title 31 of the Code of Federal Regulations is proposed to be amended as follows:

**PART 103 – FINANCIAL RECORDKEEPING AND REPORTING OF
CURRENCY AND FINANCIAL TRANSACTIONS**

1. The authority citation for part 103 continues to read as follows:

Authority: 12 U.S.C. 1829b and 1951-1959; 31 U.S.C. 5311-5314 and 5316-5332; title III, sec. 314 Pub. L. 107-56, 115 Stat. 307.

2. Subpart B of part 103 is amended by adding new § 103.11(ddd) to read as follows:

§ 103.11 Meaning of terms.

* * * * *

(ddd) *Loan or finance company.* A person engaged in activities that take place wholly or in substantial part within the United States in one or more of the capacities listed below, whether or not on a regular basis or as an organized business concern. This includes but is not limited to maintenance of any agent, agency, branch, or office within the United States. For the purposes of this paragraph (ddd), the term “loan or finance company” shall include a sole proprietor acting as a loan or finance company, and shall not include a bank, a person registered with and functionally regulated or examined by the Securities and Exchange Commission or the Commodity Futures Trading Commission, or an individual employed by a loan or finance company or financial institution under this part.

- (1) *Residential mortgage lender or originator.* For purposes of this part:

(i) *Residential mortgage lender.* The person to whom the debt arising from a residential mortgage loan is initially payable on the face of the evidence of indebtedness or, if there is no such evidence of indebtedness, by agreement, or to whom the obligation

is initially assigned at or immediately after settlement. The term “residential mortgage lender” shall not include an individual who finances the sale of the individual’s own dwelling or real property.

(ii) *Residential mortgage originator.* A person that takes a residential mortgage loan application and offers or negotiates terms of a residential mortgage loan for compensation or gain.

(iii) *Residential mortgage loan.* A loan that is secured by a mortgage, deed of trust, or other equivalent consensual security interest on: i) a residential structure that contains one to four units, including, if used as a residence, an individual condominium unit, cooperative unit, mobile home or trailer; or ii) residential real estate upon which such a structure is constructed or intended to be constructed.

3. Subpart B of part 103 is amended by adding new § 103.14 to read as follows:

Sec. 103.14 Reports by loan or finance companies of suspicious transactions.

(a) *General.* (1) Every loan or finance company shall file with FinCEN, to the extent and in the manner required by this section, a report of any suspicious transaction relevant to a possible violation of law or regulation. A loan or finance company may also file with FinCEN a report of any suspicious transaction that it believes is relevant to the possible violation of any law or regulation, but whose reporting is not required by this section.

(2) A transaction requires reporting under this section if it is conducted or attempted by, at, or through a loan or finance company, it involves or aggregates funds or other assets of at least \$5,000, and the loan or finance company knows, suspects, or has

reason to suspect that the transaction (or a pattern of transactions of which the transaction is a part):

(i) Involves funds derived from illegal activity or is intended or conducted in order to hide or disguise funds or assets derived from illegal activity (including, without limitation, the ownership, nature, source, location, or control of such funds or assets) as part of a plan to violate or evade any Federal law or regulation or to avoid any transaction reporting requirement under Federal law or regulation;

(ii) Is designed, whether through structuring or other means, to evade any requirements of this part or any other regulations promulgated under the Bank Secrecy Act, Public Law 91-508, as amended, codified at 12 U.S.C. 1829b, 12 U.S.C. 1951-1959, and 31 U.S.C. 5311-5314, 5316-5332;

(iii) Has no business or apparent lawful purpose or is not the sort in which the particular customer would normally be expected to engage, and the loan or finance company knows of no reasonable explanation for the transaction after examining the available facts, including the background and possible purpose of the transaction; or

(iv) Involves use of the loan or finance company to facilitate criminal activity.

(3) More than one loan or finance company may have an obligation to report the same transaction under this section, and other financial institutions may have separate obligations to report suspicious activity with respect to the same transaction pursuant to other provisions of this part. In those instances, no more than one report is required to be filed by the loan or finance company(s) and other financial institution(s) involved in the transaction, provided that the report filed contains all relevant facts, including the name of each financial institution involved in the transaction, the report complies with all

instructions applicable to joint filings, and each institution maintains a copy of the report filed, along with any supporting documentation.

(b) *Filing and notification procedures--*(1) *What to file.* A suspicious transaction shall be reported by completing a Suspicious Activity Report (“SAR”), and collecting and maintaining supporting documentation as required by paragraph (c) of this section.

(2) *Where to file.* The SAR shall be filed with the FinCEN in accordance with the instructions to the SAR.

(3) *When to file.* A SAR shall be filed no later than 30 calendar days after the date of the initial detection by the reporting loan or finance company of facts that may constitute a basis for filing a SAR under this section. If no suspect is identified on the date of such initial detection, a loan or finance company may delay filing a SAR for an additional 30 calendar days to identify a suspect, but in no case shall reporting be delayed more than 60 calendar days after the date of such initial detection.

(4) *Mandatory notification to law enforcement.* In situations involving violations that require immediate attention, such as suspected terrorist financing or ongoing money laundering schemes, a loan or finance company shall immediately notify by telephone an appropriate law enforcement authority in addition to filing timely a SAR.

(5) *Voluntary notification to FinCEN.* Any loan or finance company wishing voluntarily to report suspicious transactions that may relate to terrorist activity may call the FinCEN's Financial Institutions Hotline in addition to filing timely a SAR if required by this section.

(c) *Retention of records.* A loan or finance company shall maintain a copy of any SAR filed by the loan or finance company or on its behalf (including joint reports), and the original (or business record equivalent) of any supporting documentation concerning any SAR that it files (or is filed on its behalf), for a period of five years from the date of filing the SAR. Supporting documentation shall be identified as such and maintained by the loan or finance company, and shall be deemed to have been filed with the SAR. The loan or finance company shall make all supporting documentation available to FinCEN or any Federal, state, or local law enforcement agency, any Federal regulatory authority that examines the loan or finance company for compliance with the Bank Secrecy Act, or any state regulatory authority that examines the loan or finance company for compliance with state law requiring compliance with the BSA upon request.

(d) *Confidentiality of SARs.* A SAR, and any information that would reveal the existence of a SAR, are confidential and shall not be disclosed except as authorized in this paragraph (d). For purposes of this paragraph (d) only, a SAR shall include any suspicious activity report filed with FinCEN pursuant to any regulation in this part.

(1) *Prohibition on disclosures by loan or finance companies—(i) General rule.* No loan or finance company, and no director, officer, employee, or agent of any loan or finance company, shall disclose a SAR or any information that would reveal the existence of a SAR. Any loan or finance company, and any director, officer, employee, or agent of any loan or finance company that is subpoenaed or otherwise requested to disclose a SAR or any information that would reveal the existence of a SAR, shall decline to produce the SAR or such information, citing this section and 31 U.S.C. 5318(g)(2)(A)(i), and shall notify FinCEN of any such request and the response thereto.

(ii) *Rules of construction.* Provided that no person involved in any reported suspicious transaction is notified that the transaction has been reported, paragraph (d)(1) of this section shall not be construed as prohibiting:

(A) The disclosure by a loan or finance company, or any director, officer, employee, or agent of a loan or finance company of:

(1) A SAR, or any information that would reveal the existence of a SAR, to FinCEN or any Federal, state, or local law enforcement agency, any Federal regulatory authority that examines the loan or finance company for compliance with the Bank Secrecy Act, or any state regulatory authority that examines the loan or finance company for compliance with state law requiring compliance with the BSA; or

(2) The underlying facts, transactions, and documents upon which a SAR is based, including disclosures to another financial institution, or any director, officer, employee, or agent of a financial institution, for the preparation of a joint SAR; or

(B) The sharing by a loan or finance company, or any director, officer, employee, or agent of the loan or finance company, of a SAR, or any information that would reveal the existence of a SAR, within the loan or finance company's corporate organizational structure for purposes consistent with Title II of the Bank Secrecy Act as determined by regulation or in guidance.

(2) *Prohibition on disclosures by government authorities.* A Federal, state, local, territorial, or tribal government authority, or any director, officer, employee, or agent of any of the foregoing, shall not disclose a SAR, or any information that would reveal the existence of a SAR, except as necessary to fulfill official duties consistent with Title II of the Bank Secrecy Act. For purposes of this section, official duties shall not

include the disclosure of a SAR, or any information that would reveal the existence of a SAR, to a non-governmental entity in response to a request for disclosure of non-public information or a request for use in a private legal proceeding, including a request pursuant to 31 CFR 1.11.

(e) *Limitation on liability.* A loan or finance company, and any director, officer, employee, or agent of any loan or finance company, that makes a voluntary disclosure of any possible violation of law or regulation to a government agency or makes a disclosure pursuant to this section or any other authority, including a disclosure made jointly with another institution, shall be protected from liability for any such disclosure, or for failure to provide notice of such disclosure to any person identified in the disclosure, or both, to the full extent provided by 31 U.S.C. 5318(g)(3).

(f) *Compliance.* Loan or finance companies shall be examined by FinCEN or its delegates under the terms of the Bank Secrecy Act, for compliance with this section. Failure to satisfy the requirements of this section may be a violation of the Bank Secrecy Act and of this part.

(g) *Applicability date.* This section applies to transactions initiated after an anti-money laundering program required by section 103.142 of this part is required to be implemented.

4. Subpart I of part 103 is amended by adding new § 103.142 to read as follows:

Sec. 103.142 Anti-money laundering programs for loan or finance companies.

(a) *Anti-money laundering program requirements for loan or finance*

companies. Each loan or finance company shall develop and implement a written anti-money laundering program that is reasonably designed to prevent the loan or finance company from being used to facilitate money laundering or the financing of terrorist activities. The program must be approved by senior management. A loan or finance company shall make a copy of its anti-money laundering program available to the Financial Crimes Enforcement Network, or its designee upon request.

(b) *Minimum requirements.* At a minimum, the anti-money laundering program shall:

(1) Incorporate policies, procedures, and internal controls based upon the loan or finance company's assessment of the money laundering and terrorist financing risks associated with its products and services. Policies, procedures, and internal controls developed and implemented by a loan or finance company under this section shall include provisions for complying with the applicable requirements of subchapter II of chapter 53 of title 31, United States Code and this part, integrating the company's agents and brokers into its anti-money laundering program, and obtaining all relevant customer-related information necessary for an effective anti-money laundering program.

(2) Designate a compliance officer who will be responsible for ensuring that:

(i) The anti-money laundering program is implemented effectively, including monitoring compliance by the company's agents and brokers with their obligations under the program;

(ii) The anti-money laundering program is updated as necessary; and

(iii) Appropriate persons are educated and trained in accordance with paragraph (b)(3) of this section.

(3) Provide for on-going training of appropriate persons concerning their responsibilities under the program. A loan or finance company may satisfy this requirement with respect to its employees, agents, and brokers by directly training such persons or verifying that such persons have received training by a competent third party with respect to the products and services offered by the loan or finance company.

(4) Provide for independent testing to monitor and maintain an adequate program, including testing to determine compliance of the company's agents and brokers with their obligations under the program. The scope and frequency of the testing shall be commensurate with the risks posed by the company's products and services. Such testing may be conducted by a third party or by any officer or employee of the loan or finance company, other than the person designated in paragraph (b)(2) of this section.

(c) *Compliance.* Compliance with this section shall be examined by FinCEN or its delegates, under the terms of the Bank Secrecy Act. Failure to comply with the requirements of this section may constitute a violation of the Bank Secrecy Act and of this part.

(d) *Effective date.* A loan or finance company must develop and implement an anti-money laundering program that complies with the requirements of this section on or before the later of six months from the effective date of the regulation, or six months after the date a loan or finance company is established and becomes subject to the requirements of this section.

5. Subpart I of part 103 is amended by deleting § 103.170(b)(1)(ii).

6. Subpart I of part 103 is amended by redesignating § 103.170(b)(1)(iii) as § 103.170(b)(1)(ii).

7. Subpart I of part 103 is amended by redesignating § 103.170(b)(1)(iv) as § 103.170(b)(1)(iii).

8. Subpart I of part 103 is amended by redesignating § 103.170(b)(1)(v) as § 103.170(b)(1)(iv).

9. Subpart I of part 103 is amended by redesignating § 103.170(b)(1)(vi) as § 103.170(b)(1)(v).

10. Subpart I of part 103 is amended by redesignating § 103.170(b)(1)(vii) as § 103.170(b)(1)(vi).

11. Subpart I of part 103 is amended by redesignating § 103.170(b)(1)(viii) as § 103.170(b)(1)(vii).

12. Subpart I of part 103 is amended by redesignating § 103.170(b)(1)(ix) as § 103.170(b)(1)(viii).

13. Subpart I of part 103 is amended by redesignating § 103.170(b)(1)(x) as § 103.170(b)(1)(ix).

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Dated: _____

James H. Freis, Jr.
Director,
Financial Crimes Enforcement Network